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CEO's advice to his successor: Dear Archibald

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A CEO'S ADVICE TO HIS SUCCESSOR

Dear Archibald....

by J. PAUL LYET/Chairman, CEO, Sperry Corporation

The interaction between the chief executive officer and his corporation's board of directors varies widely from company to company. It is my feeling, however, that there are critical fundamentals which every CEO should follow in working with his board. I offer them in the following letter to my as yet undesignated successor.

Dear *Archibald,*

Although you have participated in board meetings and observed our preparations for them, I think it is important to pass on to you my thinking about the interrelationship between the CEO and the board. You may use it in fashioning your own approach.

First and foremost: never take the board for granted. Of course I should have no concern about your attitude. You will know that you have the job because you have the board's confidence. But you also will be conscious of the fact that you have yet to demonstrate by your performance that its trust is well placed. This will come with time. In fact, it is only after you are firmly in control of your operation that you will become susceptible to a dangerous "mindset": taking the board for granted. In other words, never let the trappings of office dull your awareness of who put you in the job—that you are basically an "employee" and that your "boss", the board, can move you out of that spot in an instant.

Next, maintain the philosophy that there is not time at board meetings to cover all the good things about the company. Consequently, focus on the critical areas—the problems and the opportunities that we face. The good news will creep in anyhow. Use the available time to make certain that the board is informed fully about any problems.

No Surprises

A fundamental rule should be never to surprise the board. To avoid that here at Sperry, we have structured our internal communications to minimize that possibility. The fact that you might have been surprised by, let us say, the sudden need for a large write-off will not be regarded by the board as an excuse for surprising them. The early warning signs clearly would be evident to someone in the corporation much earlier.

Also, never spring major proposals on the board and seek its immediate approval. If you have known about the likelihood of the proposal for months ahead—and that is usually the case—it will be evident to the board as well. If members are placed in a position where their refusal would hurt the company, and if they are given insufficient time to consider the project, you will have placed them in an unfair position and will have made a withdrawal from your "confidence account" with the board.

Acquisitions provide a splendid example of the "early warning" system. Thus, as you know, we have made it a practice to tell the board in advance of their meeting about any possible acquisition, and we update them with the situation each month. The net result is that when we are ready to recommend an acquisition to the board, a positive decision will be much more likely. By then, the board will have provided its input, and we, in turn, will have reacted to that input.

Some companies are reluctant to send the agenda, complete with supporting documentation for the subjects to be discussed, to board members in advance. Similarly, at the conclusion of a meeting, they also gather up everything which has been distributed. Some justify this approach with examples of leaks that they, or other companies, have experienced.

Our practice is different, as you know. In all of my board experience, I have never known of a leak. I urge you to continue to send complete information to the board in advance of the meetings. Continue to provide them with the complete monthly financial management report that we prepare for ourselves at the corporate level. Continue to let them retain, as I consider to be their right, *all* the information we provide to them (save the earnings projections which, for obvious reasons, they have elected to return). Continue to send the board, at the beginning of the year, a list of the items we have scheduled for each monthly meeting so that *they* have an opportunity to suggest items. And continue to provide each director who is absent an informal written account of what happened at the meeting, in addition to the regular minutes.

The board is one of the corporation's most valuable resources. Its members are immensely successful people. They are bright, articulate, experienced, and interested. The value we receive from their services is far greater than the compensation that is given to them for the services they provide.

The board's presence means that my chances for making a mistake on a major decision are minimized considerably, since I will have the benefit of its opinions as well as those of my associates. The chances that we *all* will be wrong are minimal. This is not to suggest any abdication of your fundamental accountability for operating results. However, each member of our board is uniquely qualified to give sound advice. Don't wait for the board meeting to ask for it. In fact, most of the benefits from board relationships may come between meetings. Members are always glad to offer assistance, to have the opportunity to make a contribution.

Finding Your Successor

From the day you succeed me, you can be certain that the board will be interested in management succession—and properly so. Otherwise, your sudden absence from the scene would place upon them the burden of making the decision on a successor with less information than they are entitled. At the first meeting of the personnel and organization committee, advise its members on how you appraise your associates in management, and from time to time keep the entire board informed as well. I can understand a possible reluctance to indicate a preferred successor at this point, so I would urge you to provide the senior member of the board with an "only if" letter that sets forth the alternatives as you saw them at the time you wrote the letter—reserving, of course, the right to change your mind. As a side benefit, dialogue will facilitate decisions concerning compensation for the individuals involved.

At some point you are going to be faced with the need for a new director. Remember, however, that the selection process is up to the nominating committee. Be glad that it is. Some boards rely on the chief executive to recruit new directors. In most cases, however, I think it is impertinent for the chief executive to announce to the board that a particular person has been approached and would be willing to serve if it is determined that he is acceptable to the board. That puts the board in a most awkward position. In one situation I know of, the chief executive's candidate was not approved, and the chief executive was faced with the need to go back to the person that he had approached.

Undoubtedly the nominating committee will want your suggestions for persons to add to the list already accumulated. Apart from the obvious, let me suggest some things that you *not* do. Don't recommend a friend, someone you think for certain will agree with you because of the similarity of your viewpoints. In the short run it might be comfortable, but may I remind you that you honestly can suggest only those persons you are certain would vote for your removal should the circumstances warrant it.

One of the most competent chief executives I know also happens to be one of my closest friends. Some years ago, he asked me to go on his board, and I declined solely because of the friendship. Later, when an opening

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on our board developed, several directors recommended him as a candidate, and I opposed it for the same reason.

Now you and I know that friendships with board members *do* develop. That is normal, natural, and it would be unrealistic to expect otherwise. The distinction is subtle, but it is nonetheless there. For you will find that as your friendship develops, the director will never allow his relationship with you to compromise the objectivity of his decisions affecting you or the company.

More Suggestions

Now, a few thoughts about some other matters relating to the board. Keep in mind that our mandatory retirement age for directors is 70. If you appoint a new director who has just a few years to serve, you will likely find yourself needing to replace that director at about the time when the person has finally "tuned in." On the other hand, if you name a director who has, say, 25 years of possible service remaining, you may encounter a different problem. Your appraisal of the director's interest and capabilities, even his probable career path, may prove erroneous. With the passage of time, people do change.

With respect to board size, it has been my experience that a relatively small board works out most advantageously. It facilitates informality and participation, and it obviates the need for a plethora of committees.

Also remember, when you are running the meetings, that the directors expect them to start promptly and to end at approximately the time you have indicated. Frequently they have scheduled commitments that are integrated with the time slot of our board meeting.

In addition, remember that not all directors will speak up on a given subject. Some may have reservations on a subject but may not consider them—or the subject—sufficiently important to raise an objection, particularly when it appears that the consensus of the board is moving in the other direction. With critical matters especially, do not call for a final vote until you have sought the opinions of all who have been silent. When board members know that it is likely that they will be called upon if they don't speak up, you will find that these directors will do so without reticence.

Also keep in mind that the board needs the reassurance of getting to know others in management. I recommend that you continue the practice of having the officers present for the "non-executive" board session.

In addition, make certain that board members get to know the people running the divisions. When division heads come in for presentations, make sure the board has pictures and a biography of each one.

And don't forget this: making a presentation to a board is often a considerable strain for those not accustomed to doing it. It is up to you to create an atmosphere in which they can be relaxed. I would strongly urge that they have an opportunity to make a "dry run." Thus, you and the principal officers will know approximately how long the presentation should last and will be in a position to evaluate whether or not the board is likely to be interested in what is being covered. You then may also tell the presenter which questions are most likely to be asked.

Finally, I urge you to continue to be a strong proponent for a minimum of inside board members. There will always be pressures to "reward" competent internal performance with board membership. Resist it. Should you succumb, you will have opened a Pandora's box. The purpose of the board is not to provide a status vehicle for management. There will never be enough available seats, and the disincentive for those who aspire, but remain unseated, is certain to be a problem for you.

When a board is comprised of a majority of inside members, the outside members are in a difficult position. In a sense, they are the captives of management. This is theoretical, I grant you, because perceptive management will often recognize the position of the outside board member and create a de facto majority position for the outsiders through its own deference.

Nevertheless, in reality the board consists of the chief executive officer and the outside board members, because the insiders will usually vote as a unit with the chief executive. Thus, the CEO certainly could prevail in a difference of opinion with the outside directors. I suspect, however, that the number of competent outside directors who would be content to be overruled in such situations, particularly where major questions are involved, would be few indeed.

Finally, Be Yourself

There are undoubtedly a number of items which I have forgotten to include in this epistle, but I know that you will fashion your own approach and reshape it as circumstances warrant. But if these rambling observations prove to be helpful, I shall be very pleased—just as I am for having had the opportunity to submit them to you.

Sincerely,

Paul

J. PAUL LYET